AUDITOR GENERAL
Alberta

Report of the Auditor General of Alberta

November 2006

Alberta Alcohol and Drug Abuse Commission
- Contracting practices

Aboriginal Affairs and Northern Development
- Referral to the Chief Electoral Officer
- Métis Settlements Ombudsman

Infrastructure and Transportation
- Capital grants to Métis Settlements

Lakeland College
- Contracting practices

Post Secondary Institutions
- Contracting practices
- General computer controls

Agriculture, Food and Rural Development
- Expense accounts

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Ms. Janis Tarchuk, MLA
Chair
Standing Committee on Legislative Offices

I am honoured to send my report titled "Report of the Auditor General—November 2006" to the members of the Legislative Assembly.

I intend to make this report public on November 23, 2006.

Fred J. Dunn, FCA
Auditor General

Edmonton, Alberta
November 20, 2006

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Snapshot

Results of six systems audits

We are reporting the results of six audits that were not ready for the October 2006 *Annual Report of the Auditor General*. We normally report our work once a year, but the lessons to be learned regarding the purpose of controls in maintaining integrity are worthy of immediate consideration.

Lessons learned

a. **Hire wisely and then supervise**—good practices and systems can ensure the right people are hired. They can also detect developing problems and reduce the risk of undetected problems growing. Effective government systems depend on the integrity and skills of the people who use them (see AADAC and Lakeland).

b. **Segregate incompatible job duties**—no one person should be responsible for the administration of a contract. Segregating duties is a necessary control (see AADAC and Lakeland).

c. **Monitor contract results**—it's not enough to sign a contract and then hope it will administer itself. Someone has to actively monitor contract results. In these audits, we found ineffective review and oversight. Effective contract management is essential to maintain integrity and achieve value for money (see AADAC, Lakeland and Aboriginal Affairs).

d. **Monitor terms and conditions of grants**—parties that give conditional grants have to ensure recipients meet the conditions. Otherwise, the grant conditions are meaningless (see Infrastructure and Transportation).

e. **Sign construction contracts (interim or final) before the work starts**—otherwise, there's inadequate control of risks. Prohibit donations during the contract-tendering process—to avoid favoritism and the appearance of it (see Grant MacEwan and SAIT).

f. **Inform staff about how to report alleged employee misconduct**—and when allegations are made, ensure management deals with them promptly and consistently (see Agriculture, Food and Rural Development).

g. **Ensure independence and impartiality of those that investigate**—without these qualities, an Ombudsman, for example, loses effectiveness and authority. If objectivity is the key to success, then the government must create organizational structure that will accomplish that expectation (see Aboriginal Affairs).

h. **Take the necessary steps to protect computer systems**—organizations depend on computerized financial and other information systems to conduct their business. They must assess the risk of loss of quality, availability and confidentiality of their information against the cost of its protection—and then put the right controls in place (see post secondary institutions).

Alberta Alcohol and Drug Abuse Commission (AADAC)—Contracting practices

Findings	Recommendations	Risks	Lessons learned
Because AADAC did not properly segregate job duties, a senior employee was able to divert $634,000 from 5 contracts.	• Segregate job duties and monitor contract results properly. • Verify credentials of prospective employees. • Ensure management reports to the Board annually on the effectiveness of internal controls.	Fraud, wasted money, missed contract objectives, employee misconduct.	Even minor controls contribute to important ends. Due diligence needed in checking prospective employees. No one person should have sole control of a contract.

Aboriginal Affairs and Northern Development—Métis Settlements Ombudsman

Findings	Recommendations	Risks	Lessons learned
The Métis Settlement Ombudsman (MSO) entered into a contract inconsistent with the principle of MSO independence and created a potential conflict of interest. The Department did not effectively manage its contract with the MSO.	Review MSO role to: • ensure contract is adequately monitored and managed to meet objectives, or • establish MSO Office under *Métis Settlement Act*, or • provide ombudsman services in another independent and impartial way.	MSO's credibility diminished. Purpose of independent MSO not met.	Ombudsman must be—and be seen to be—independent and impartial. Department must monitor MSO contract results.

Infrastructure and Transportation—Capital grants to Métis Settlements

Findings	Recommendations	Risks	Lessons learned
The Department does not have effective systems to monitor and ensure compliance with program requirements and conditions of certain grants to Métis Settlements. Considerable non-compliance is the result.	Implement risk-based system to ensure grant recipients comply with grant conditions.	Money spent for non-program purposes. Grant conditions meaningless.	Conditional grants don't manage themselves—someone has to manage them to ensure grants are spent properly, according to their conditions.

Lakeland College—Contracting practices

Findings	Recommendations	Risks	Lessons learned
Lakeland College contracting processes and supervision of contracting staff do not follow best practices.	Improve contracting practices, supervision of contracting staff, and monitoring of individual contracts.	Non-compliance with contracts, damage to College's reputation, inadequate information for decisions.	Good practices and systems can ensure the right people are hired and then supervised. They can also detect developing problems and reduce the risk of undetected problems growing.

Post Secondary Institutions—Contracting practices

Findings	Recommendations	Risks	Lessons learned
Grant MacEwan College and Southern Alberta Institute of Technology both failed to have signed construction contracts for more than 6 months after major construction projects started.	Sign contracts (interim or final) before construction starts.	Construction risks not managed.	Contracts (interim or final) for construction projects must be signed before construction starts.
MacEwan accepted $250,000 from a party bidding on a contract. That party won the contract.	Don't solicit or accept donations during contract-tendering process.	Perception of preferential treatment and conflicts of interest.	Donations from parties bidding to win a contract create perception problems.

Agriculture, Food and Rural Development—Expense accounts

Findings	Recommendations	Risks	Lessons learned
The Department does not have processes for reporting and dealing with alleged employee misconduct.	Improve system for reporting and dealing with employee misconduct.	Employee misconduct goes unreported. Inconsistent and unfair treatment of allegations—valid allegations ignored and necessary action not taken.	Staff need to know how to report alleged misconduct. Management needs to respond to alleged employee misconduct—promptly and consistently.

Alberta Alcohol and Drug Abuse Commission (AADAC)—Contracting practices

See page 14

Internal controls—Recommendation No. 1

We recommend that management improve controls over contracting by:

- ensuring adequate segregation of duties exists over the contracting process
- monitoring and verifying contractors' compliance with contract terms and conditions

Management response

Accepted. AADAC has taken steps to enhance its financial processes to ensure adequate segregation of duties and has put in place additional monitoring of the terms and conditions of contracts, including the establishmen. of an internal Contracts Review Committee.

See page 16

Academic credentials and criminal records check—Recommendation No. 2

We recommend that:

- for prospective employees, AADAC verify credentials such as university diplomas with granting institutions
- AADAC ensure criminal records checks are completed in accordance with their policy

Management response

Accepted. AADAC has instituted new procedures to verify all credentials with granting institutions and ensure compliance with the Commission's policy on criminal record checks.

See page 17

Board governance—Recommendation No. 3

We recommend that the Board, at least annually, receive reports from management on the design and effectiveness of AADAC's internal controls.

Management response

Accepted. The Audit Committee and the Board currently receive reports on internal controls and risk management. We will now ensure that this occurs on an annual basis.

Aboriginal Affairs and Northern Development—Métis Settlements Ombudsman

See page 21

Role of Métis Settlements Ombudsman—Recommendation No. 4

We recommend the Department of Aboriginal Affairs and Northern Development review how it handles the Métis Settlements Ombudsman role and:

- ensure any contract for ombudsman services is adequately monitored and managed to ensure government objectives are achieved, or
- establish an Office of the Métis Settlements Ombudsman in accordance with the *Métis Settlements Act* with corresponding regulations, or
- provide ombudsman services under other such processes or options that maintain the principles of independence and impartiality.

Management response

Accepted. The Department of Aboriginal Affairs and Northern Development is currently working on an implementation plan to address the recommendation. The implementation plan will be completed in 2007.

Infrastructure and Transportation—Capital grants to Métis Settlements

See page 24

Capital grants to Métis Settlements—Recommendation No. 5

We recommend that the Department of Infrastructure and Transportation implement an effective risk-based system to ensure that recipients of Rural Transportation Grants and Street Improvement Program grants comply with the terms and conditions of those grants.

Management response

Accepted. The Department of Infrastructure and Transportation will implement a more effective risk-based system to ensure that recipients of the Rural Transportation Grants and the Streets Improvement Program grants comply with the terms and conditions of those grants.

Lakeland College—Contracting practices

See page 30

Contract policies and procedures—Recommendation No. 6

We recommend that Lakeland College review and amend its contract management procedures to follow best practice, including, but not limited to:

- conducting background checks on companies that are not known to the College prior to entering into contracts
- updating policy to require employees to disclose conflicts of interest
- providing guidance on monitoring performance against contract terms
- retaining only final signed version of contracts

Management response

Accepted. We will review our contract management procedures and amend them as necessary. We expect to implement the recommendation by January 31, 2007.

See page 31

Monitoring performance—Recommendation No. 7
We recommend that Lakeland College improve supervision of its contracting staff.

Management response
Accepted. As noted in the auditor's findings, numerous meetings and corrective e-mails supplemented by formal evaluation all took place with the former General Manager of Business and Industry Training. Recognizing that there were some issues, management further improved supervision by performing the following:

- *As of July 1, 2006 a new position, Director of Extension Services, was created to oversee the operations of Business and Industry Training and other extension programming.*

Supervision of the General Manager of B.I.T. was always present and increased in July. It is also important to note in the auditors' findings that there were no concerns expressed by any of the parties contracting with the College. We will implement additional reporting and monitoring measures to further improve supervision of contracting staff beginning in January 2007.

We also recommend that Lakeland College monitor its contract performance against contract terms, and profitability of individual contracts in the Business Unit.

Management response
Accepted. We will implement this recommendation by January 31, 2007.

See page 34

International students—Recommendation No. 8
We recommend that Lakeland College enforce its policy for involvement with international students.

Management response
Accepted. We will commit to train all deans, directors and appropriate managers at their council meetings. This will take place by January 31, 2007.

Post Secondary Institutions

See page 35

Grant MacEwan College construction management—Recommendation No. 9
We recommend Grant MacEwan College ensure that signed contracts (interim or final) for construction projects are in place before projects start.

Management response
Accepted. Improvement should be made in the timing of contract signing relative to commencement of services. While various parameters may not allow for absolute contract completion prior to service commencement, significant delays should not be incurred. Policies will be adjusted to ensure advance services and delays in contract signing are minimized.

See page 37

Donations to Grant MacEwan College—Recommendation No. 10

We recommend that Grant MacEwan College establish a policy clearly indicating it will not solicit or accept donations with participating vendors during a tendering process.

Management response

Accepted. Procurement policy will be adjusted to ensure the College avoids any conflict of interest, real or perceived, by disallowing bidders from providing donations or gifts to the College during the tender process.

See page 39

Southern Alberta Institute of Technology construction management—Recommendation No. 11

We recommend the Southern Alberta Institute of Technology ensure signed contracts (interim or final) are in place for construction projects prior to services being rendered.

Management response

Accepted. Management will investigate industry standard practices for construction contracts, report back to its Campus Development and Audit Committees and effect the necessary changes to SAIT's practices.

Agriculture, Food and Rural Development—Expense accounts

See page 46

Processes for reporting and dealing with allegations of employee misconduct—Recommendation No. 12

We recommend that the Department of Agriculture, Food and Rural Development improve its systems for reporting and dealing with allegations of employee misconduct.

Management response

Accepted. The Department will work to develop and implement a policy which will outline appropriate processes for reporting and responding to allegations of employee misconduct.

Alberta Alcohol and Drug Abuse Commission (AADAC)—Contracting practices

Summary

Five false contracts totalling $634,250

From January 1, 2004 to September 15, 2006, a senior AADAC employee (Lloyd Carr, the Executive Director[1] responsible for the Tobacco Reduction Unit (TRU)), through the use of five false contracts, diverted AADAC funds totalling $441,298 to himself and $192,952 to other parties. He was successful in diverting the funds because he was able to take advantage of weaknesses and circumvent controls in AADAC's contracting system. We found no evidence that other parties knowingly supported the Executive Director in diverting the funds from these contracts. The RCMP Commercial Crime Section is conducting a criminal investigation as a result of a complaint by AADAC. Further, AADAC is working with Alberta Justice Civil Law Branch to consider what civil remedies may be available to it.

Our examination focused mainly on the circumstances surrounding the five contracts. Although we did not do a complete review of internal controls and board governance, we did identify opportunities for management to improve internal controls over contracts and for the AADAC Board to improve its governance practices over internal controls and human resources.

Improved monitoring of contracts and segregation of duties required

We recommend that management improve the segregation of duties over the contracting process and improve its monitoring and verification of contractors' compliance with contract terms and conditions. We also recommend that the AADAC Board receive, at least annually, reports from management on the design and effectiveness of AADAC's internal controls.

Verification of credentials required

Our examination also found that the Executive Director did not possess the credentials he claimed in his original 1997 employment application to AADAC and that he had a criminal record at the time of his application. AADAC did not verify the credentials he claimed in his application before hiring him. AADAC required the Executive Director to undergo a criminal records check when he was promoted in 2005. However, he did not do so and AADAC did not follow up with

[1] Lloyd Carr was, until he was terminated in September 2006, the Executive Director of AADAC Specialized Services, which oversees the Tobacco Reduction Unit. He was promoted to this position effective December 2005. Previously, he was the Senior Manager leading the Tobacco Reduction Unit. Throughout this report, we refer to him as the Executive Director.

him to determine why. We recommend that AADAC ensure criminal record checks are completed as required by their policy.

While checking credentials for employment applications or obtaining criminal records checks may seem like bureaucratic exercises, in this situation, the completion of either of these tasks may have identified a potential problem. If AADAC had obtained this information, the problem with the contracts may not have arisen because AADAC may not have hired the individual. But if AADAC had hired him, it may have learned of his criminal record when he was considered for promotion in 2005 and the subsequent losses may have been lessened.

Audit scope and objectives

Focus of contracts examined at TRU

We examined all TRU contracts for 2005–2006. These 66 contracts totalled approximately $2.1 million. As a result of that work, we also examined certain TRU contracts for 2003–2004 and 2004–2005. In some cases, we interviewed individuals that had entered into contracts with AADAC. We also obtained documents from other organizations or individuals outside of AADAC on either a voluntary basis or used our powers under the *Auditor General Act*. We did not examine contracts administered by other AADAC programs. Our objective was to determine if value was received for payments made by AADAC under contracts administered by TRU, and if contracting received sufficient oversight from senior management and the Board.

Background

As an agency of the Government of Alberta, AADAC operates and funds information, prevention and treatment services to help Albertans with alcohol, other drug and gambling problems. A Board of Directors appointed by the Lieutenant Governor in Council provides oversight. The CEO directs the day-to-day operations of AADAC and reports to the Board.

In March 2002, Alberta introduced the Alberta Tobacco Reduction Strategy, giving AADAC the mandate to lead and co-ordinate tobacco reduction efforts on behalf of the government. This mandate led to the establishment of the Tobacco Reduction Unit. TRU has a 2006–2007 annual budget of approximately $4.2 million and consists of six employees led by a Senior Manager reporting to the Executive Director, who in turn reports to the Vice President, Provincial Services. The Vice President reports to the CEO. To meet its objectives, TRU contracts with health professionals, not-for-profit organizations, researchers, consultants, advertising organizations and other service providers.

During our 2005–2006 AADAC financial statement audit, a concern was brought to our attention by AADAC's Senior Financial Officer that there was little or no documented evidence of contract deliverables for a particular TRU contract. Subsequent audit work together with AADAC staff assistance indicated unusual aspects to a number of contracts that required follow up by us.

Our audit findings and recommendations

1. Examination of contracts

First false contract with ASH. Funds flowed to Executive Director's bank account

In January 2004, the Executive Director arranged a contract for $9,750 with Action on Smoking & Health (ASH), an Edmonton based not-for-profit organization, for a public awareness campaign on smoking in the City of St. Albert. ASH was influenced by the Executive Director to use a third-party consultant from St. Albert to provide the services. ASH representatives had no explanation why AADAC did not contract directly with the third-party consultant rather than having the funds flow through ASH. A total of $9,500 flowed from AADAC through ASH into the Executive Director's bank account. ASH retained a $250 handling fee. There was no work done by the third-party consultant relative to this contract.

Four false contracts with AB Lung

From June 2004 to September 2006, the Executive Director administered four contracts with the Alberta Lung Association (AB Lung). From AADAC's perspective, these contracts provided funds to AB Lung for the delivery of a purported senior-high school tobacco reduction program (the school program).

We compared the contracts at AADAC to the contracts held by AB Lung for the school program. The contracts were different. The AB Lung contracts contained the same dates, contract numbers, payable amounts and authorizing signatures as the AADAC contracts. However, the AB Lung contracts identified different contractor payees and did not describe the school program. The AB Lung contracts identified capacity building and a billboard campaign to be completed by:

- Kilburn and Associates (Kilburn), an independent consulting firm that had a prior business relationship with AADAC.
- Out of the Box Consulting, a non-corporate entity controlled by the Executive Director.
- Debora Corr (a fictitious name), identified with the same home address as the Executive Director.

No work performed. Funds flowed to Executive Director's bank account

We determined that AB Lung made contract payments to each of these entities and retained a handling fee, as outlined in their version of the contract, for doing so. We also determined that Kilburn paid the funds it received from AB Lung back to the Executive Director, less a handling fee.

There was no evidence that AB Lung or Kilburn were expected to complete, or in fact completed, any work, other than passing funds through their books and bank accounts.

Executive Director's explanation to AB Lung and Kilburn

Neither AB Lung nor Kilburn knew anything about the school program, which in reality did not exist. We understand that the Executive Director told AB Lung that AADAC distances itself from certain tobacco reduction activities at municipal levels of government. It is also our understanding that the Executive Director told Kilburn that AB Lung wanted the Executive Director to do consulting work, but that a corporate entity was required, which the Executive Director did not have. Both AB Lung and Kilburn considered these explanations by the Executive Director at the time to be reasonable, and therefore did what he asked them to do.

In carrying out these contracts, it appears that AB Lung and Kilburn did not communicate with each other or anybody at AADAC other than the Executive Director. We found no evidence that ASH, AB Lung or Kilburn knowingly supported the Executive Director in diverting the funds from these contracts.

Following is a synopsis of payments for these five contracts:

Contract #	Funds advanced by AADAC	ASH handling fees	AB Lung handling fees	Kilburn handling fees	Funds to Executive Director	Totals
1	$9,750	$250			$9,500	$9,750
2	$99,500		$20,000	$2,802	$76,698	$99,500
3	$130,000		$20,000	$29,500	$80,500	$130,000
4	$195,000		$20,000	$20,400	$154,600	$195,000
5	$200,000 Note A		$80,000 Note B	Nil	$120,000	$200,000
Totals	**$634,250**	**$250**	**$140,000**	**$52,702**	**$441,298**	**$634,250**

Note A—only $200,000 of $225,000 total (on each contract version) was forwarded by AADAC to AB Lung.

Note B—AB Lung is currently holding these funds.

Examination conducted to follow the funds

Using our powers under the *Auditor General Act*, we traced funds diverted to AB Lung, Kilburn and the Executive Director. We conducted extensive interviews and examined bank documents, credit card records, mortgage documents, land title records, motor vehicle records, credit histories, public records of political contributions, e-mail messages from AADAC e-mail accounts and other records located on AADAC premises. We followed up in each instance that suggested the purchase of an asset or the movement of funds to another person or organization. On the basis of this examination, we concluded that:

- AB Lung received $140,000 of which $60,000 was used in its operations. It currently holds the remaining $80,000.
- Kilburn received $52,702 and used it in its operations. We reviewed sufficient information to conclude that Kilburn completed no transactions with these funds that were worthy of further follow-up.
- The Executive Director spent $91,000 as a down payment on a new house, $60,000 on a vehicle loan repayment[2] and withdrew approximately $156,000 in cash from ATMs, of which $116,000 was from ATMs located in casinos. These ATM withdrawals were typically between $300 and $900 each. We also confirmed that the Executive Director was a regular customer at a casino located in his home community.
- The remaining diverted funds (approximately $134,300) appear to have been intermingled with family income to support the Executive Director's lifestyle from 2004 to 2006.

Executive Director admits gambling problem

We interviewed the Executive Director. He told us he had a gambling problem and confirmed his involvement in the five contracts as described in this report. The pattern and location of ATM withdrawals and information from casino staff is consistent with the Executive Director's claim of a gambling problem. He also stated that he believes that Kilburn and AB Lung thought the contracts and transactions were legitimate.

Allegations of contributions to provincial leadership contenders unsupported

A member of the public advised us that there was information on the Internet[3] that AADAC funds from these contracts may have been provided to tobacco control lobbyists who then provided the funds to the campaigns of provincial leadership contenders. We also had two other witnesses advise us independently that the Executive Director had aspirations to more senior positions within government. Accordingly, we considered if funds may have been diverted to a political party or candidate for political office, in order to enhance career aspirations or other opportunities. We found nothing to support these allegations.

[2] See page 16.

[3] See: http://surrealitytimes.blogspot.com/—we confirmed that the information brought to our attention was unchanged as of November 17, 2006.

Diverted funds not used for political contributions

We questioned the Executive Director about this issue during our interview, and we examined his financial records for evidence of donations to political organizations or candidates. The Executive Director stated that he did not use any of the diverted funds to make political contributions and his records did not show any such contributions. We also questioned Kilburn and AB Lung about political contributions. They each indicated that none of the funds in question were used for political purposes. As previously indicated, we concluded that these organizations used the funding for their operations.

We also reviewed records at the Office of the Chief Electoral Officer. We could find no evidence of any political contributions from any person or entity identified during this audit. Unlike some jurisdictions, contribution records for leadership campaigns in Alberta are not required to be publicly available. However, this is a matter for the Legislative Assembly to consider. In any event, we have no evidence that any of the diverted funds were used for political purposes.

2. Examination of internal controls

AADAC needs to improve controls

As a result of our findings related to these five contracts, we decided to look further at internal controls over the contracting process. We also considered the oversight provided by the AADAC Board, specifically concerning internal control and human resource matters. We concluded that there are opportunities for AADAC to improve controls and governance practices. The following recommendations are provided to strengthen internal controls in AADAC.

Recommendation No. 1

We recommend that management improve controls over contracting by:

- **ensuring adequate segregation of duties exists over the contracting process**
- **monitoring and verifying contractors' compliance with contract terms and conditions**

Background

To meet its mandate, AADAC enters into contracts for goods and services and has procedures in place for contracting. First, a program area must identify a need and ensure funding is available. The second phase is to plan the scope and nature of the contract. The contract should identify what AADAC will receive under the contract. For service contracts, the contractor may be required to submit progress reports.

AADAC's contract policy

AADAC has procedures to ensure that there is sufficient review prior to approving the contract. An Expenditure Officer signs off indicating sufficient funds are available. The Program Manager signs to indicate the requirement

of the contract is clearly defined and if required, a competitive process has been used to award the contract. A Finance Officer signs confirming that the terms of reference and payment are clear. The size of the contract may require additional senior management signoff by the Executive Director, Vice President or CEO.

Three copies of the final contract are prepared for signing. The contracts are initially signed by the required AADAC officials and then forwarded to the contractor for signatures. The contractor keeps one copy and sends the other two back to AADAC—one for the program area and one for Finance.

The manager of the unit or the contractor supervisor is responsible to ensure the terms and conditions of the contract are met. Once AADAC is satisfied the conditions of the contract have been met, payment for the invoice is approved. Upon completion of the contract, an evaluation checklist, as well as copies of the final report from the contractor must be submitted prior to the final invoice being paid.

Criteria: the standards we used for our audit

There should be an adequate system of internal control that mitigates AADAC's risk of inappropriate diversions of funds.

Our audit findings

Executive Director controlled contracts and directed payments

We found little or no interaction by AADAC employees or management, other than the Executive Director, in the administration of the five TRU contracts identified in this report. Contract payments to ASH and AB Lung were in all cases approved by the Executive Director, reviewed and coded by an Expenditure Officer directly supervised by the Executive Director, then sent to Finance for payment. For the five contracts administered by the Executive Director, there was no evidence of delivery of the required services in AADAC files. Had other employees been involved with oversight of the contracts and/or involved in periodic discussions with the contractors, this diversion of funds may not have occurred or would have been detected earlier. Similarly, if the contractors' compliance with contract terms and conditions had been monitored more effectively, by someone independent of the Executive Director, it is likely that this matter would have surfaced much earlier than it did, with a potentially smaller loss to AADAC.

Executive Director authorizes payments of approximately $1.4 million to an advertising vendor. No contract in place

In addition to the above mentioned five contracts, we found evidence that the Executive Director administered payments of approximately $1.4 million per year for advertising services. These payments were made pursuant to letters of intent between AADAC and Sports & Entertainment Inc. and signed on behalf of AADAC by only the Executive Director. The amounts of these letters of intent exceeded the Executive Director's financial authority, which was $75,000. Invoices, sometimes totalling over $380,000 were received

directly by the Executive Director, initialled and forwarded to the same Expenditure Officer who processed the ASH and AB Lung contract payments. The Expenditure Officer would review and code the invoice, then forward it to Finance for payment. Payments should not have been made without an approved contract in place. Although this was a breakdown of internal controls, we did not have sufficient evidence to conclude that value for money was not obtained from this supplier.

Executive Director receives $60,000 loan from advertising vendor

We did find, based on evidence obtained at AADAC, that the Executive Director received a payment of $60,000 in 2005 from Sports & Entertainment Inc. Our subsequent interviews and review of documents led us to conclude that this $60,000 payment was in fact a loan to the Executive Director to purchase a new vehicle. We also located evidence that the Executive Director subsequently paid the loan back, interest free, to Sports & Entertainment Inc. with funds diverted from AADAC. At the very least, the acceptance of a loan on favourable terms from a major supplier is inappropriate, a conflict of interest and contrary to AADAC's Code of Ethics.

3. Academic credentials and criminal records check

Recommendation No. 2

We recommend that:

- **for prospective employees, AADAC verify credentials such as university diplomas with granting institutions**
- **AADAC ensure criminal records checks are completed in accordance with their policy**

Background

AADAC needs to validate credentials

AADAC receives applications for employment in its Human Resources Department. As would be expected, applications would typically include a resume of experience and evidence of credentials such as diplomas and degrees. In some cases, evidence of a criminal records check is required with an employment application or promotion to a new position.

Criteria: the standards we used for our audit

- Information in employment applications should be verified prior to an offer of employment.
- Criminal records checks should be performed of prospective and current employees for positions where evidence of criminal activities would present an unacceptable risk to AADAC.

Our audit findings

Executive Director does not have university degree as outlined in his personnel file

We located records that indicated the Executive Director was not a graduate of a Bachelor of Social Work program from the University of Calgary, as had been claimed on his AADAC job application from 1997. We confirmed with the University of Calgary that it had no record of the Executive Director

being a graduate of their university. If, in 1997, AADAC had validated the credentials claimed by the Executive Director, the employment application in all likelihood would not have proceeded and the Executive Director would not have had the opportunity to divert funds.

Executive Director did not submit criminal record check for his promotion. No follow up by AADAC

We also found documentation in the Executive Director's desk at AADAC that indicated he had a criminal record. During our interview with the Executive Director, he confirmed to us that he had a criminal record when he applied to AADAC for employment in 1997 and that he did not tell AADAC of its existence. He was requested to provide a criminal record check when he was promoted to Executive Director in December 2005. However, he did not provide the results of the check to AADAC and no one at AADAC followed up with him to determine why the criminal records check had not been provided. We extended our examination to include a sample of criminal records checks for other senior employees. We found no instances requiring follow-up.

4. Board Governance

Recommendation No. 3

We recommend that the Board, at least annually, receive reports from management on the design and effectiveness of AADAC's internal controls.

Background

Under the *Alcohol and Drug Abuse Act*, the AADAC Board consists of up to twelve members appointed by the Lieutenant Governor in Council. Members of the Board, other than the chair and vice-chair, are appointed for terms of up to three years and may be re-appointed for a second three-year term. The Board is chaired by a Member of the Legislative Assembly and currently consists of the chair, vice-chair and nine members. The Board provides policy direction for AADAC's programs and services.

Criteria: the standards we used for our audit

Generally, Boards oversee the processes that management has in place to identify and manage business opportunities and risks. They monitor management's systems and processes for identifying and managing risks. This will include assessing the framework of internal control established by management.

The Canadian Institute of Chartered Accountants has defined control as "a process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations.
- Reliability of internal and external reporting.
- Compliance with applicable laws and regulations and internal policies."

Our audit findings

Based on our interviews with the Chair of the AADAC Board and the Chair of the Audit Committee, and an examination of Board minutes, we found the Board to be primarily engaged in providing policy direction to management. The Board does not regularly obtain information from management on the design and effectiveness of AADAC's internal controls.

Independent review conducted on internal controls

Assessing and reporting on the adequacy of internal controls is the responsibility of management. In March 2005, management contracted with an independent consultant to perform an internal controls review. The consultant recommended to management that they improve controls over:

- Safeguarding confidential information
- Segregation of duties
- Payroll reconciliations
- Controls over revenue contracts and grants
- Inventory count procedures
- Controls over grant applications
- Administration of contracts

Board provided a copy of independent review

This report provided management with information on the design and effectiveness of certain internal controls and is a useful first step in a process to report to the Board on internal control. Management did provide a copy of this consultant's report to the Board.

Board needs to be more involved in governance issues

Management needs to ensure that all key controls are identified, evaluated as to their effectiveness, and the results of the evaluation reported to the Board. This should include controls for:

- internal and external financial reporting
- performance reporting
- compliance with human resource policies, including policies for conflicts of interest
- reporting of employee ethics violations and fraud

Aboriginal Affairs and Northern Development

1. Referral to the Chief Electoral Officer

Summary

We received a complaint from a member of a Métis Settlement that corporations wholly owned by Métis Settlements had made contributions to Minister Pearl Calahasen's 2004 provincial election campaign, contrary to the *Election Finances and Contributions Disclosure Act*. After interviewing the complainant and reviewing publicly available documents, we concluded there was sufficient information to refer the matter to the Chief Electoral Officer for his review and action.

2. Métis Settlements Ombudsman

Summary

Public complaint the MSO impaired his credibility

We received a complaint from a member of a Métis Settlement (the Settlement) that in July 2004, the Settlement paid the Métis Settlements Ombudsman (MSO) under a fee-for-service contract to conduct an investigation in the community. This contract—at the very least—put the MSO in a potential conflict-of-interest position, impaired his credibility, and compromised his ability to be independent. The contract required the MSO to accept direction on the investigation from the elected Settlement Council (the Council).

MSO function must remain independent and impartial

Fairness, independence and impartiality are key characteristics of the Ombudsman function as it exists in Canada and around the world. To maintain an effective MSO function for the Métis communities, the Department must ensure that the MSO meets and maintains these characteristics.

Audit scope and objectives

Our objectives for this audit were to determine if:

- the MSO entered into a fee-for-service contract as alleged. If so, assess whether the contract could affect the perception of his ability to discharge his duties in a fair, independent, and impartial manner.
- the Department's contract management processes were adequate to ensure government objectives were achieved.

Background

The *Métis Settlements Act* (the Act) authorizes the Minister of Aboriginal Affairs and Northern Development (the Minister) to make regulations establishing the Office of the Métis Settlements Ombudsman, as well as the terms and conditions of an Ombudsman appointment.

Ombudsman services provided by a company under contract

Although section 175.1 of the Act allows the Minister to establish the Office of the Métis Settlements Ombudsman, she has not done so. Nor has she made any regulations. Instead, the government, represented by the Minister, contracted in 2003 with a corporation, MSO Services Inc., to have it act as MSO. The Minister delegated inspection and investigation powers described in sections 171, 172, 174 and 175 of the Act to the MSO through Ministerial Order to the sole shareholder of MSO Services Inc.

The MSO should provide an impartial and independent review of complaints about Métis Settlements' management and leadership. The MSO role is described in his annual report as follows:
"...to provide an independent and impartial place to take complaints about Settlements management or leadership. It also exists to identify unfair or unjust complaints made against Councils and staff".[1]

MSO not to do other work without Department approval

Under his contract with the Department, the MSO cannot carry on any other work while acting as the MSO—unless the Department provides written consent. The Department funds MSO operations and there is no provision or requirement for individuals or communities to pay either the MSO or the Department for MSO services.

[1] Métis Settlements Ombudsman 2005–2006, Annual Report, page 8

Our audit findings and recommendations

Role of Métis Settlements Ombudsman

Recommendation No. 4

We recommend the Department of Aboriginal Affairs and Northern Development review how it handles the Métis Settlements Ombudsman role and:

- **ensure any contract for ombudsman services is adequately monitored and managed to ensure government objectives are achieved, or**
- **establish an Office of the Métis Settlements Ombudsman in accordance with the *Métis Settlements Act* with corresponding regulations, or**
- **provide ombudsman services under other such processes or options that maintain the principles of independence and impartiality.**

Our audit findings

The MSO worked under direction of a Settlement Council

We substantiated the allegation that the MSO entered into a fee-for-service contract under the direction of the Council. We found no evidence of written consent by the Department for this work and no evidence that the Minister allocated costs under the Act for such an investigation.

The MSO told us that the Council asked him in July 2004 to perform specific investigative duties that fell within his mandate. However, he felt he did not have adequate resources to complete the tasks and asked for direction and funding from the Department. The MSO said that his contact at the Department told him that if the Settlement wanted an investigation as described, they should pay for it themselves. He then entered into a contract with the Settlement and had a sub-contractor perform the work under his direction. The MSO then billed the Settlement for approximately $16,000.

MSO and Department have differing views on whether Department consented to the work

We were unable to assess if the MSO formally requested additional funding from the Department or if he sought the Department's consent before work began. The MSO and senior Department staff had differing views of the actual discussions that took place. However, the Department staff member responsible to monitor the MSO contract told us that he was aware of the MSO's contract with the Settlement and reported it to his supervisor.

The Department failed to consider the potential for impairing the MSO's credibility

Despite this knowledge at a senior level in the Department, no one took formal steps to assess whether the MSO's contract with the Settlement impaired his credibility or his ability to continue fulfilling his duties in accordance with his contract and the principles that should govern an ombudsman.

MSO contract with the Settlement doesn't support the perception of independence

These circumstances, together with the terms and conditions of the MSO's contract with the Settlement, are inconsistent with the principle of independence—nor do they support the perception of independence. We considered the following terms and conditions of the MSO's contract with the Settlement:

- The MSO must consult, advise and accept direction from the Settlement Council.
- All writings or other property created, developed or gathered as a result of the MSO's services under the contract are the property of the Settlement and must be delivered to the Settlement upon request.
- The information acquired by the MSO as a result of the contract must be held in strict confidence and not disclosed without the written consent of the Settlement.
- The MSO agrees to indemnify the Settlement against any third-party claims, demands and actions for which the MSO is legally responsible, and the MSO acknowledges responsibility for any loss or damage to Settlement property due to the MSO's omission or negligence.

The Department needs to review how it provides ombudsman services

Accordingly, we concluded that the Department should review the MSO role. The Department needs to ensure that Settlements can access appropriate, independent and impartial ombudsman services, with sufficient oversight to ensure the role functions according to its mandate.

Implications and risks if recommendation not implemented

The credibility of the MSO's work may be diminished, and the objective of an effective MSO may not be achieved if the Department's processes and contract with the MSO do not adequately cover matters of independence, impartiality, and conflict of interest.

Infrastructure and Transportation—Capital grants to Métis Settlements

Summary

Grant conditions not enforced

Based on an allegation from a member of a Métis Settlement that a conditional grant from the Department of Infrastructure and Transportation was not used in accordance with the terms and conditions of the grant, we reviewed grants under the Street Improvement Program (SIP) and Rural Transportation Grants (RTG). The grants we reviewed were provided by the Department to the eight Métis Settlements in Alberta between 2004 and 2006. Collectively, these grants totalled approximately $3 million. Although the Department has established terms and conditions for grant funding, we found that some conditions were rarely enforced by the Department.

Audit scope and objective

Our objective was to determine if the Department has adequate systems and processes in place to ensure that money paid to Métis Settlements is used according to the terms and conditions governing the grants. We plan to follow up in the future and expand our scope to review grants provided to other municipalities.

Background

The Department provides financial assistance to Métis Settlements for capital-related transportation, water and wastewater systems, and core municipal infrastructure needs. The SIP and RTG programs help Settlements engineer, plan, design, construct, and maintain roads. Funding is based on formulas that include things like population, kilometres of open road, and terrain.

The Department requires applications for SIP grants to describe the proposed work, including detailed cost estimates, proposed construction schedule, and location plans. Applications for grants under the RTG program may be made by way of a letter, and must contain a listing of proposed work for the upcoming year. If the Department approves an application, it pays the money to the Settlement. Under each program, a Settlement must invest the grant money to maximize interest and use the interest to reduce the cost of the work. SIP grant recipients must publicly advertise for tenders and private contractors for the construction. There is no tendering requirement under the RTG program, but 50% of eligible costs must be spent on private sector contractors.

Recipients must report work done

Annually, Settlements must report on the use of money they receive by submitting to the Department a Statement of Funding and Expenditures, which must include the following information:

- a summary of work completed, including costs,
- unused funds carried forward from the prior year or funds to be carried forward into the following year,
- the amount of interest earned on grant funds invested during the year.

Our audit findings and recommendations

Capital grants to Métis Settlements

Recommendation No. 5

We recommend that the Department of Infrastructure and Transportation implement an effective risk-based system to ensure that recipients of Rural Transportation Grants and Street Improvement Program grants comply with the terms and conditions of those grants.

Our audit findings

The department is not enforcing grant conditions

There is only limited evidence that the Department requires recipients to comply with grant terms and conditions; there was considerable non-compliance with grant terms and conditions in 5 of the 8 Settlements whose grants we reviewed. Our findings relate to both programs and are summarized below. We found:

- inconsistencies in the level of detail of the proposed work. The level of detail was often not sufficient to identify the scope of the work. Applications contained general descriptions of the proposed work, for example, "road construction" or "gravelling" and lacked detailed cost estimates, location plans, and proposed construction schedules.
- a lack of documented evidence of using private contractors to complete eligible work—only 3 of the 8 Settlements provided it.

Funds not deposited into separate bank account

- only 1 of the 8 Settlements was depositing money into a separate, interest-bearing account as required under each grant program. Any revenue earned from the investment of grant funds is to be deducted from eligible costs before the grant calculation is made. There was no evidence that the Department monitored or enforced this requirement.

Department is not inspecting work done

- no evidence that the Department had a process to review grant applicant financial records or inspect work under the programs. A Department employee told us that, although random spot checks are carried out, none had been conducted in recent memory for Métis Settlement applications.

Funding provided without reports

- documents indicating that at least three recipients were three or more years behind in their reporting, but still received funding based on proposed work. The Department sends out annual reminder letters requesting outstanding reports. However, the letters do not say that further funding depends on receiving this information. In some cases, the Department approved retroactive funding for grants even though there was no evidence that eligible work was completed—or even contemplated—in the prior years. We found no Department policy on retroactive applications.

Implications and risks if recommendation not implemented

Without adequate controls to ensure that conditional grant money is used according to terms and conditions, applicants have no incentive to spend public money for program purposes. In effect, conditions for the funding become meaningless.

Lakeland College—Contracting practices

Summary

Request to review contracts between the College and Kihew

In early October 2006, local media reported that 35 Polish welders (the workers) were employed full time for Edmonton-area companies even though they had entered Canada on student visas to attend a full-time program at Lakeland College. We were asked by the Department of Advanced Education and the Board of Governors of Lakeland College to review contracts between the College and Kihew Energy Services Ltd. because available information suggested that the College had a contractual relationship with Kihew to provide training to the workers. When we began our work, we learned that the RCMP Immigration and Passport Section was already investigating the circumstances surrounding the workers' arrival in Canada, as well as their relationship with several Alberta businesses. This investigation is still ongoing at the time of our report.

Focus was on the College's contracting practices

Accordingly, our audit did not include a review of immigration matters or any potential contractual, employment or other issues between the workers and Alberta companies. Rather, we focused on Lakeland's administration of contracts.

4 contracts examined

We examined four contracts the College entered into with Kihew. Each contract covered a separate group of foreign nationals. These contracts require the College to provide, for a fee ($3,870–$5,600 per student), safety, English-as-a-second-language (ESL), and either welding or machinist training to each of the four groups of foreign nationals.

The College did not meet contractual requirements

The four contracts we examined were negotiated and administered by the former General Manager of the Business and Industry Training Department (the Business Unit). He was also the sole signatory on two of these contracts. The College did not meet all of its contractual requirements in the contracts with Kihew. This happened because the College:

- does not have adequate contracting procedures
- did not effectively supervise the former General Manager of the Business Unit
- did not monitor its performance against the terms of the contracts

College sent letters to Citizenship and Immigration Canada

We also reviewed the College's involvement with issuing letters to Citizenship and Immigration Canada in support of student visa applications and found that the College's policies and practices were not followed. These letters indicated that the foreign nationals would be full-time students of the College for 52 weeks. The College had a training plan that covered ESL, class-time, and

experience with practicum businesses for the 52-week program. However, the College had little contact with practicum providers and did not provide supervisory assistance to students while on practicum, which was a significant portion of the program to be delivered. The College was therefore unable to ensure that the students were receiving the appropriate training as required by the program.

Number of students involved unknown

It is not clear how many students were involved. Management told us they sent 158 letters to Citizenship and Immigration Canada, but could only provide evidence of 84 letters. They also told us that some foreign nationals that had arrived in Canada had already returned to Poland. We have not interviewed any of the foreign nationals.

We also have not interviewed the former General Manager of the Business Unit or the General Manager from Kihew.

Audit scope and objectives

Foreign nationals have concerns about completion of education program

In September 2006, approximately 35 foreign nationals met with Thomas Lukaszuk, Member of the Legislative Assembly for Edmonton—Castle Downs. They were concerned that they were not completing their educational program in accordance with the conditions of their student visas. Their concerns went to the Minister of Advanced Education. On September 19, 2006, the Department of Advanced Education asked us to review the contracts between the College and Kihew.

Our objective was to determine if the contracts signed by the Business Unit of the College followed good contracting practice for delivering services.

To do this, we:

- interviewed College staff
- examined contracts between the College and Kihew
- interviewed staff from the four companies that provided practicum training (practicum providers) to the foreign nationals
- examined other evidence at the College of training activities provided to the foreign nationals and monitoring of the contracts
- examined other information provided to us

We did not examine how the foreign nationals were recruited or the immigration process. And we did not examine any transactions between Kihew and the foreign nationals or between Kihew and the practicum providers. As noted, the RCMP are investigating these matters.

We received full cooperation and assistance from the College staff and from the staff of the four practicum providers.

We have not been able to interview the former General Manager of the Business Unit or the General Manager from Kihew. We are currently in discussions with each of their lawyers and may be conducting interviews with them in the near future.

As the RCMP investigation proceeds, we will continue to monitor this matter.

Criteria: the standards we used for our audit

- The College should have documented contracting policies and procedures that contractors understand and comply with
- The contract should contain a sound framework for contract management and accountability
- Contracting staff should be competent
- Contracting performance should be monitored and acted on
- Conflict-of-interest guidelines should be in place and complied with
- Contracting should be cost-effective

Background

The College operates under the *Colleges Act* and is board-governed. It has campuses in Lloydminster and Vermilion and a Learning Centre in Strathcona County. The Business Unit is located in Strathcona County.

College objectives—respond to regional needs and prepare people for future

The College's primary objectives are to respond effectively to regional emerging needs, and to prepare people for a future in the global community. The Business Unit is part of the continuing education program at the College. The College expects the Business Unit to make a profit.

Business Unit objective—prepare workers for trades certification

The objective of the Business Unit is to prepare workers for trades' certification through Alberta Apprenticeship and Industry Training. On behalf of the College, the Business Unit seeks contracts with industry to develop and deliver customized industry training in various fields, including basic welding.

Former General Manager negotiated contracts

The former General Manager of the Business Unit, on behalf of the College, negotiated four contracts with Kihew. The contracts were for the College to provide four separate 52-week programs for groups of up to 25 students—supplied by Kihew. Three welding programs were to start in January, March and June, 2006 and one machinist program was to start in March 2006. Foreign nationals arrived in Canada in January, March, and May 2006.

Contractual requirements

The contracts with Kihew require the College to:

- deliver welding training and provide students with necessary materials for their courses
- provide Worker's Compensation Benefits (WCB) coverage for the students during their practicum
- provide supervisory assistance while the students were on practicum
- make arrangements with Alberta Apprenticeship and Industry Training for exam writing and pay the exam fees for the first 25 students
- assist in hiring instructors to teach ESL, safety, welding or machinist theory and labs

International student processes

The College has a formal process for dealing with international students:

1. the student applies to the College
2. the College assesses the student's qualifications against its criteria
3. if the student is accepted, the College sends two letters to the student; one provides information to the student about acceptance, fees etc.; the other letter is for the student to use for student visa purposes

The Admissions Office has been delegated the authority to sign the letters sent to international students. The College's process does not include sending letters directly to Citizenship and Immigration Canada.

Our audit findings and recommendations

1. Contract policies and procedures

Recommendation No. 6

We recommend that Lakeland College review and amend its contract management procedures to follow best practice, including, but not limited to:

- **conducting background checks on companies that are not known to the College prior to entering into contracts**
- **updating policy to require employees to disclose conflicts of interest**
- **providing guidance on monitoring performance against contract terms**
- **retaining only final signed version of contracts**

Our audit findings

The College has a documented contract management policy. However, the policy is limited to guidance on where to send draft contracts, where signed contracts should be filed, and levels of signing authority. The policy does not cover, for example, management practices for drafting contracts and forms, contracting knowledge requirements for staff, or monitoring performance against contract terms.

No background check on Kihew

The College did not perform background checks on Kihew to ensure that it was appropriate to do business with the company. Kihew's website does not contain any phone numbers or addresses for the company. Because the address for Kihew is a post office box in Goodfish Lake, we made inquiries in the Goodfish Lake area and were unable to find a physical location for the company.

No requirement for disclosure of conflicts of interests

The College's guidelines on conflict of interest are included in the Code of Conduct. The guideline does not require staff to disclose potential conflicts of interest so that the College can determine whether it should remove the individual from the decision making process.

Poor contracting practices

In addition to not having adequate contracting policies and procedures, we also found the following poor practices in our review of the contracts with Kihew:

- multiple drafts of signed and unsigned contracts
- signatures and dates on draft contracts
- notations on signed contracts that appeared to be alterations to the original contract terms
- use of a standard template that was insufficient

Implications and risks if recommendation not implemented

Inadequate contracting procedures increase the risk that the College staff may not follow appropriate contracting practices.

The College faces increased risk:

- of fraudulent activities
- that it will not comply with all contractual terms

2. Monitoring performance

Recommendation No. 7

We recommend that Lakeland College improve supervision of its contracting staff.

We also recommend that Lakeland College monitor its contract performance against contract terms, and profitability of individual contracts in the Business Unit.

Our audit findings

Former General Manager had history of non-compliance with College policies

Management at the College recognized that the former General Manager was not consistently complying with College policies. His supervisor and College support departments (registrar's office, human resources and finance) contacted him on several occasions to ask him to comply with College policies. On July 1, 2006 the College created and filled the position of Director of Extension Services to oversee the Business Unit. Management also exercised a clause in the former General Manager's contract to terminate his employment on October 4, 2006.

Former General Manager not adequately supervised

Further, for the contracts we examined, we did not find any evidence that the former General Manager was adequately supervised. Without any independent review, he was able to:

- negotiate four contracts with Kihew on behalf of the College
- send letters directly to Citizenship and Immigration Canada
- make all billing decisions in relation to the Kihew contracts
- miss deliverables from the terms of the contracts

2 of 4 contracts not appropriately authorized

He did not have the authority as defined in the College's policy to issue letters in support of student visa applications. Two of the four contracts were not approved by the College's appropriate levels of signing authority. The two contracts that were approved were subsequently amended by the former General Manager without approval. We found no evidence that his actions on these contracts were specifically questioned by management.

College did not comply with all contractual terms

The College did not complete all of the tasks it was contracted to provide. Nor did it monitor its compliance with the terms of the contracts. The following is a summary of the key contractual requirements and the College's performance against them:

Under the contract the College was required to:	Did the College meet the requirement?
deliver welding training and provide students with necessary materials for their courses	Not yet required— Instructors were hired to provide welding training scheduled to start September 27, 2006, under the Business Unit's original training plan. No students attended the College to take this training.
provide Worker's Compensation Benefits coverage for the students during their practicum	Yes
provide supervisory assistance while the students were on practicum	No

Under the contract the College was required to:	Did the College meet the requirement?
make arrangements with Alberta Apprenticeship and Industry Training for exam writing and pay the exam fees for the first 25 students	Not yet required—College staff told us that arrangements need to be made only two months in advance of the exam.
assist in hiring instructors to teach ESL, safety, welding or machinist theory and labs	Partially—ESL instructors were hired and we were able to confirm that 16 foreign nationals received ESL training. Management told us that ESL training was delivered to all students who showed up to take it.

We found no evidence that any lack of performance was identified or reported to relevant College authorities.

College billed for services it did not deliver

The College billed for services that it had not delivered. Even though the College had not provided all of the training required under the January 2006 contract, and fewer than the maximum 25 students participated in the program, it billed Kihew for the full amount of the contract.

For the March and May 2006 contracts, the College has not been able to provide evidence that all the students it billed for were participating in the program. No training was provided to any students under these contracts. Kihew paid the College $215,465—the full amount the College billed for all of the contracts.

Exact number of foreign nationals unknown

We have not been able to determine the exact number of foreign nationals or when they arrived in Canada. We received listings of the foreign nationals from the College and from the four practicum sites. The College also gave us a list of the foreign nationals that it received from Kihew. We were unable to reconcile the differences in the information we received.

No project budget prepared

The College did not prepare a project budget before the contracts we examined were signed. The former General Manager was responsible for the budget and profitability of the contract. We found no evidence of any ongoing review of the actual revenues and costs of the project or reporting to senior management.

Senior management and the board review the results of the entire Business Unit quarterly. If the results differ significantly from budget, they will follow up. This does not always result in reviewing the profitability of individual contracts.

Implications and risks if recommendation not implemented
The College has increased exposure to legal and financial risk, and reputation damage if it fails to meet its contractual requirements.

The College will not know if it has an unprofitable contract or whether to continue with an unprofitable contract. Also, the College may not detect or prevent suspicious activities if there are off-setting profitable and unprofitable contracts in the Business Unit.

3. International students

Recommendation No. 8

We recommend that Lakeland College enforce its policy for involvement with international students.

Our audit findings

Letters sent directly to Citizenship and Immigration Canada

The Business Unit's former General Manager told College management that Kihew asked him to send letters directly to Citizenship and Immigration Canada stating that the foreign nationals would be full time students in a 52-week program. Some of the foreign nationals were registered as full-time students of the College. However, initially, two practicum providers were not aware that the foreign nationals were students and told us they hired them as sub-contractors from Kihew. No one from the College attended the practicum provider's sites to provide supervisory assistance. We found no evidence that the former General Manager questioned why he was being asked to provide evidence that the foreign nationals were students.

2 practicum providers not aware foreign nationals were students

This is the only time that the Business Unit has been involved with the entry of foreign nationals to Canada as students. Normally, under Business Unit contracts, the College designs and provides industry training to a group of staff supplied by a company. Whether the staff are Canadian citizens or foreign nationals is not relevant to the College's willingness or ability to deliver contracted services. The Admissions Office did not sign the letters sent to Citizenship and Immigration Canada, contrary to College policy. Four individuals signed the letters: the former General Manager and three people that reported to him. Management told us that 158 letters were prepared, signed and mailed to Citizenship and Immigration Canada. However, the College could only provide evidence of 84 signed letters.

Implications and risks if recommendation not implemented
The College's risk of liability increases if inaccurate statements are made to Immigration Canada.

Post Secondary Institutions

1. Contracting practices

Summary

As part of our June 30, 2006 financial statement audits of Grant MacEwan College and the Southern Alberta Institute of Technology (SAIT), we examined contracting practices for major construction projects.

About 25% of MacEwan's $55 million Robbins Health Learning Centre was finished and nearly $14 million paid to the builder before the final contract was signed. At SAIT, about 7% the Residence III building was finished and about $3.7 million paid to the builder before the final contract was signed. Both MacEwan and SAIT need to avoid unnecessary risk and employ sound business practices by promptly finalizing contracts with builders for major projects.

MacEwan needs to handle donations better. Just days before the Robbins Health Learning Centre tendering process closed, MacEwan publicly announced it had received $250,000 from an active bidder in that same tendering process. That donor went on to win the contract to construct the Health Learning Centre. We found that the bid selection process was proper and not affected by the publicly announced donation. However, MacEwan needs to avoid actual or perceived conflicts of interest by not soliciting or accepting donations from participants in open tendering processes.

1.1 Grant MacEwan College construction management

Recommendation No. 9

We recommend Grant MacEwan College ensure that signed contracts (interim or final) for construction projects are in place before projects start.

Background

Construction of the Robbins Health Learning Centre (the Centre) started in November 2005 with an expected completion date of September 2007. MacEwan selected Clark Builders as design-builder through a public tendering process. In a November 24, 2005 letter to Clark and a December 13, 2005 purchase order, MacEwan approved a design-build contract budget plan to form the basis of a contract between MacEwan and Clark.

Criteria: the standards we used for our audit

MacEwan should have signed contracts (interim or final) in place before construction projects start.

Our audit findings

MacEwan paid $18.1 million over 10 months with no contract in place

MacEwan and Clark did not sign the design-build stipulated price contract until the end of September 2006. As of September 30, 2006, the Centre was approximately 25% complete and MacEwan had paid $13.9 million to Clark and $4.2 million to various consultants.

MacEwan assessed the risks it identified, while construction was ongoing and no contract was in place. A letter of intent, purchase order, schedule and compliance certificate with the RFP requirements were issued. MacEwan also completed a risk assessment to determine the impact of:

- The builder deviating from technical and design requirements
- The builder withdrawing from the project
- The builder not complying with the construction schedule
- An injury or accident causing physical damage

Risks were identified and managed

To manage these risks, MacEwan took steps such as retaining a 10% holdback on all payments, assessing their campus insurance coverage and requiring from the builder:

- A performance bond, builders risk and bodily injury / property insurance, sub-contractor statutory declarations and WCB coverage
- Regular meetings to assess progress and adherence to design
- Review of builder invoices by the project architect
- Monthly property lien checks to check for legal actions against the project

Ten months construction without a contract is excessive

While MacEwan appears to have managed the risks it identified, sound business practices in administering public funds require a more timely execution of the final contract. Some delay in finalizing a contract may be expected, but we believe the delay of some ten months and payments exceeding $18 million to be excessive.

Implications and risks if recommendation not implemented

Without a signed contract prepared by adequately instructed legal counsel and based on sound business practices, MacEwan may not adequately contemplate and manage all risks associated with the construction of public buildings.

1.2 Donations to Grant MacEwan College

Recommendation No. 10

We recommend that Grant MacEwan College establish a policy clearly indicating it will not solicit or accept donations with participating vendors during a tendering process.

Background

Following a 2003 public tendering process, Clark Builders was selected to construct a $37.5 million student residence on MacEwan's Edmonton campus. A grand opening was held on September 2, 2005 and students moved in on September 3, 2005.

MacEwan accepted $250,000 from a bidder in an active public tendering process

On September 8, 2005, MacEwan's Board of Governors was advised by its construction oversight committee that Clark had provided MacEwan with a cheque for $250,000 and that the Minister of Advanced Education had advised that government would match the commitment.[1]

On September 23, 2005, a public tender closed for the construction of the $55 million Robbins Health Learning Centre (the Centre) to be built on MacEwan's Edmonton campus. Clark was one of the two short-listed candidates. The request for tender documents included a requirement for the bidder to include "donations and other contributions" as value added items to the tender.[2] The request for tender documents did not explain why this was required. On November 21, 2005, MacEwan selected Clark to construct the Centre.

Criteria: the standards we used for our audit

MacEwan should avoid actual or perceived conflicts of interest caused by donations, or soliciting of donations, from participants during open tendering processes.

Our audit findings

The $250,000 transaction

It is not clear whether the $250,000 from Clark was a donation or a negotiated reduction in the final cost of the student residence. Interviews with management of both Clark and MacEwan support the idea that, during 2003 final contract negotiations on the student residence (but before construction began) there was a difference between what MacEwan was willing to pay and what Clark would accept. To progress the project, Clark proposed that a $250,000 payment be provided to MacEwan as a donation. MacEwan agreed and the project moved forward.

[1] Grant MacEwan Board of Governors meeting minutes—September 8, 2005

[2] Grant MacEwan College, Request for Proposal, Robbins Health Learning Centre 2005—Page 122

The $250,000 was not a donation and no cheque was ever issued. It was a negotiated price reduction

However, no cheque was actually ever issued by Clark to MacEwan; instead, Clark reduced its final invoice for the residence by $250,000 in August 2005. MacEwan management recorded the transaction as a $250,000 reduction in the cost of the residence—not a donation. We agree with this accounting treatment.

Despite the announcement by the Minister of Advanced Education that the government would match the $250,000, MacEwan did not apply for matching funds, nor are they planning to. We also understand that MacEwan did not issue a tax receipt for the $250,000. Again, we agree that MacEwan should not seek matching dollars or issue a tax receipt.

Effect of the transaction on the tendering process

We found no connection between the $250,000 transaction and the subsequent awarding of the Centre contract, though the timing of the transaction and the public announcement create the appearance that the two events could be related.

Bidders required to disclose past or intended donations

However, we found the requirement that the bidder include "donations and other contributions" as a value added item, to be unusual. We would expect the tender documents to require bidders to disclose planned donations to address potential conflicts of interest. However, we would also expect a clear statement that such transactions would have no effect on the decision to award future contracts and that MacEwan would not accept donations from bidders during a tendering process. There were no such statements in the request for tender documents.

We considered whether the $250,000 transaction may have influenced the selection process for the Centre. We engaged an independent and experienced consultant and asked that they review and consider:

- The original tender documents, including the successful and unsuccessful bids, complete with drawings
- The final contract
- Final drawings for the building currently under construction
- Bid evaluation reports prepared by MacEwan's consultants on the successful and unsuccessful bids.

Our consultant performed a review of the tendering process and certain components of the bids, but not a complete audit. On the basis of that review, our consultant concluded that:

- Bid evaluation reports prepared by MacEwan's consultants demonstrated that reasonable decisions were made on the basis of relevant criteria.

- Changes in design between the final building and what Clark originally proposed were sufficiently documented, reasonable and did not suggest weakness in the tendering process

Accordingly, we conclude that the $250,000 transaction and the awarding of the Centre contract are not linked.

Implications and risks if recommendation not implemented

The perception of preferential treatment must be avoided

The circumstances surrounding these events may lead to the perception that Clark received preferential treatment by making a significant "donation" just days before the closing of a tender in which it was participating. Whether or not the $250,000 transaction was a donation, it was reported publicly as one. With tender documents specifically asking bidders to identify donations and other contributions without clearly stating why, there may be a perception that prior or promised donations are a key factor in awarding construction contracts.

1.3 Southern Alberta Institute of Technology (SAIT) construction management

Recommendation No. 11

We recommend the Southern Alberta Institute of Technology ensure signed contracts (interim or final) are in place for construction projects prior to services being rendered.

Background

SAIT began construction of the Residence III building in February 2006 with an expected completion date of August 2007. SAIT selected Stuart Olsen as the construction manager through the public tendering process. In a November 18, 2005 letter, Stuart Olsen advised SAIT that the guaranteed maximum price for the construction cost component of the project was $42 million exclusive of GST. Subsequently, a Canadian Construction Documents Committee contract for a guaranteed maximum price of $42 million was prepared.

The Campus Development Committee is a standing committee of SAIT's Board of Governors that provides advice and recommendations to the Board with respect to the acquisition, use, renovation, upgrading or altering of SAIT's lands, buildings, and equipment. It also has oversight responsibilities for monitoring the appointment of consultants, selection of bidders and the awarding of contracts.

Criteria: the standards we used for our audit

The Institute should have legally enforceable contracts (interim or final) with contractors prior to services being rendered.

Our audit findings

We tested capital construction costs and found that SAIT and Stuart Olsen did not sign the construction management contract until the end of August 2006. As of June 30, 2006, the Residence III building was approximately 7% complete. The Institute paid Stuart Olsen $3.7 million or 9% of the guaranteed maximum price during the period when there was no signed contract in place.

SAIT implemented procedures to manage their risk associated with construction. However, we found no evidence that SAIT had assessed the risks associated with not having a signed construction management contract in place during the initial phase of construction. Furthermore, through review of the minutes, we were unable to find evidence that the Campus Development Committee was aware that there was no signed construction management contract in place with Stuart Olsen from February 2006 until the end of August 2006.

Implications and risks if recommendation not implemented

Without a signed contract prepared by adequately instructed legal counsel and based on sound business practices, SAIT may not adequately contemplate and manage all risks associated with the construction of public buildings.

2. General computer controls

Summary

Recommendations made to improve information technology controls

As part of the June 30, 2006 financial statement audits of public sector colleges, we made new recommendations to deal with the risk of IT control failure in the following eight colleges: Bow Valley College, Grand Prairie Regional College, Lakeland College, Medicine Hat College, Mount Royal College, NorQuest College, Olds College, and Portage College.

The deficiencies we identified related to management of IT risk, and protection of the information in the computer systems—see the table on page 42 for details.

Protection of information essential to colleges

Colleges depend on computerized financial and student information systems to conduct critical business activities and to generate reliable financial reporting. To protect their computerized information, colleges must properly design, document, implement, and monitor their IT controls. Our assessments followed generally accepted standards[3] that help organizations implement sound internal control over financial reporting through a reliable and auditable computing environment.

Conclusion

The management of each college needs to assess the risks—and the costs of mitigating the risks—that we identified. We recognize that the decision to accept a risk because it costs too much to mitigate is valid. If a college decides to accept risks due to cost, we expect it to document the decision and inform its oversight committees. The colleges agreed in principle with all of our recommendations.

Criteria: the IT standards we used for our audit

Colleges should have effective, documented computer controls to ensure the quality, availability and confidentiality of their information systems and the financial and student information they contain. For this summary, we have consolidated our audit work in the examination of general computer controls into the following four high-level areas:

- Risk Management
- Computer Operations and Security
- Access to Programs and Data
- Program Development and Program Change

[3] Industry standards such as COBIT and ISO 17799

Our audit findings

The following table and information summarize new IT environment audit findings reported in the management letters of the colleges that we audited. The detailed findings to the management and audit committees of the respective colleges were reported separately.

This report does not include recommendations from previous years

Colleges may have other findings or outstanding issues from previous years that are not included in this report or the table below. In previous years' audits, we made recommendations to management for colleges such as NorQuest and Portage. Conversely, this is the first year we have conducted an in-depth IT audit at Mount Royal and Medicine Hat College. As a result, there are more issues at Mount Royal and Medicine Hat College than at other colleges that have had previous, in-depth IT audits. Therefore, the number of issues in the table below is not necessarily indicative of one college having more or better IT controls than another.

We are planning in-depth IT audits of more colleges next year—they are not included here.

	Control Group	Findings	Bow Valley	Grande Prairie	Lakeland	Medicine Hat	Mount Royal	NorQuest	Olds	Portage
a.	Risk Management	No documented process to assess risks	-	X	-	X	-	-	-	-
b.	Computer Operations and Security	Inadequate security configurations	-	X	X	X	-	-	X	X
		Inadequate plans to recover from a disaster	-	-	-	X	-	-	X	-
		Inadequate Security Awareness	-	X	X	X	X	-	X	-
		Server room physical and environmental controls	-	X	X	X	-	-	-	-
c.	Access to programs and data	Inadequate user access removals and reviews	X	X	-	-	-	-	X	-
		Inadequate protection against unauthorized access	X	X	X	X	X	-	X	-
d.	Change Management	Undocumented Change Management process	X	X	X	X	X	X	X	-

Legend:
X New audit findings
- No new audit findings this year

a. Risk Management

Two colleges lacked documented control processes to periodically assess risks to their critical applications and information.

b. Computer Operations and Security

Computer systems must be protected

Five colleges lacked adequate control processes to ensure their computer systems were securely configured or to ensure that their computer systems had proper anti-virus or security updates.

Two colleges lacked adequately documented control processes or plans to recover IT operations in the case of a disaster.

Five colleges lacked adequate security awareness programs to provide initial and ongoing IT security and privacy training to students and staff.

Three colleges did not adequately protect their server rooms and have not assessed the benefits versus cost of a risk mitigation strategy. This may include inadequate fire detection and suppression, climate, or physical security controls to protect the computers that hold their sensitive student and financial information.

c. Access to Programs and Data

Access controls must be formally documented and continuously applied

Overall, we found that the eight colleges have procedures in place to request, approve, add, and terminate access to the computing network and college applications. However, these procedures were often informal, and colleges lacked evidence of continuous compliance. Without strong controls over access to programs and data, college financial and student information may be susceptible to unauthorized access.

For three colleges, we found a lack of appropriate reviews and timely termination of user access to college financial and student information systems.

At six colleges, we found inadequate controls against unauthorized access to college computer systems. Examples of weak controls included insecure network architecture, no documented roles and responsibilities to ensure segregation of duties, generic or shared IDs, weak or non-existent passwords, and accounts not being locked out after multiple unsuccessful access attempts.

d. Change Management

System changes must be approved and documented

We made new recommendations at seven colleges to document and follow an appropriate change management process. Undocumented change management processes lead to problems such as:

- Inadequate evidence that there were proper approvals prior to changes being made to the computing system.
- Inappropriate segregation of duties between the job functions that approve those changes.

Implications and risk if recommendations not implemented

Colleges may be unable to guarantee the quality, availability, and confidentiality of the financial and student information contained in their systems.

Agriculture, Food and Rural Development—Expense accounts

Summary

Systems for investigating alleged employee misconduct

We assessed the investigation by the Department of Agriculture, Food and Rural Development into the alleged misconduct of one employee involving misappropriation of assets and false expense claims. The Department took action to deal with the alleged misappropriation of assets.

Examined expense claims

In examining the alleged false expense claims, we contacted relevant third parties and found that:

Violation of Code

- the employee violated government policy by performing fee-for-service work at a College. The employee was paid $600 by the College for providing training during working hours without the approval of his supervisor.

Six claims not valid

- six claims (totalling $1,322) were either misrepresented by the employee or not confirmed by third parties.

The Department is following up on these matters with the employee and considering appropriate action.

Control systems for approving expense claims are appropriate

We also examined the Department's systems for approving employee expense claims and concluded that its systems are adequately designed and operating effectively. It is not reasonable as a matter of routine to require expenditure officers to verify expense claims with third parties, as we did—unless there are specific allegations related to an employee and their expense claims. All organizations must be able to rely on the integrity of their employees and operate with cost-effective control systems. It is impossible to completely eliminate the risk of errors or fraud in any control system.

Processes for reporting and dealing with allegations

However, the Department needs a clear process for staff to report allegations of employee misconduct. It also needs a well-understood process for investigating allegations. These processes will help the Department ensure that staff is aware of their responsibilities for reporting employee misconduct in good faith. In addition, staff will realize that the Department will take allegations seriously and deal with employee misconduct.

Audit scope and objectives

In May 2006, we received complaints from a staff member of the Department that a senior employee of the Department was inappropriately using Department assets. Subsequently, we received further complaints from another staff member of the Department that the same employee was misrepresenting their expense claims. We examined the Department's response to the allegations of employee misconduct brought to its attention.

We also examined the Department's systems for approving employee expense claims by examining the expense claims for 12 Department staff (23 claims) made between November 2005 and July 2006. Our work included assessing the appropriateness of the Department's policies for expense claims and whether the approved claims complied with the Department's policies.

Our audit findings and recommendations

1. Processes for reporting and dealing with allegations of employee misconduct

Recommendation No. 12

We recommend that the Department of Agriculture, Food and Rural Development improve its systems for reporting and dealing with allegations of employee misconduct.

Background

Deputy ministers are responsible for managing risk in their departments, including the risk of fraud. Allegations of fraud may occur in any organization, and the government is no exception.

Code of Conduct and Ethics

The Government of Alberta has a Code of Conduct and Ethics for the Public Service of Alberta that applies to all employees. The Code provides guidance to ensure that employees act with impartiality and integrity and to ensure that there not be, nor appear to be, any conflict between the private interest of employees and their duty to the public. The Department also has a Department Supplement to the Code that provides further guidance on conflict of interest to employees.

Employees annually confirm their adherence to the Code

Annually, the Department requires employees to acknowledge in writing that they have read and understood the Code and the Supplement. The Code and the Supplement both state that employees who do not comply may be subject to disciplinary action, up to and including dismissal.

PAO Guideline on Alleged Criminal Conduct

The Personnel Administration Office (PAO) has also developed the Response to Alleged Criminal Conduct by Employees guideline for departments. The purpose of the guideline is to ensure that responses to alleged employee criminal conduct are consistent and appropriate.

Criteria: the standards we used for our audit

- The Department should have policies in place for reporting and dealing with alleged employee misconduct. The policies should define the key processes and responsibilities of staff to report alleged employee misconduct and the process that management will take to investigate allegations and determine appropriate disciplinary action.

- The Department should promptly investigate allegations of employee misconduct and take appropriate disciplinary action when employee misconduct is proven.

Our audit findings

No policies or procedures

The Department does not have policies or procedures for employees to report alleged misconduct, nor does it have an established process for investigating allegations. PAO has developed a guideline for departments that covers alleged employee criminal activity, but not all types of employee misconduct. In addition, the guideline does not provide specific processes for reporting and dealing with allegations of employee misconduct.

Department action on complaints

During 2006, the Department received several complaints from staff members, both directly and through our Office, about alleged misconduct of a senior employee. The Department took action when the allegations were brought to its attention:

Reviewed expense claims

- In March 2006, the Department received complaints about the employee's behaviour. In response, the Department completed a review of the employee's expense claims made between April 1, 2005 and March 31, 2006. Because the Department did not receive any specific allegations, the review was limited to examining the claims for large or unusual expenses, or expenses that did not look appropriate given the employee's duties. The Department did not identify anything unusual and there was no evidence that the employee breached any policies.

Use of assets

- We received a complaint from a department staff member that the same employee was misappropriating Department assets and reported these allegations to the Department in June 2006. The Department examined whether all computers and other attractive assets in the employee's area were accounted for or on-site. On July 31, 2006, the Department met with the employee to ask about several missing assets, including computers, a video projector and a camera. All but one of the computers and the camera were on the premises. The employee provided the Department with reasonable explanations why a computer and the camera were not on the premises and subsequently returned these assets to the Department.

Allegations regarding expense claims

In late August 2006, we received allegations from another staff member indicating the employee was claiming mileage and meals on their expense account for travel that did not take place. In September 2006, we indicated to the Department that we intended to perform further examination of the employee's expense claims, such as verifying the claims with third parties.

31 expense claims appeared valid but further examination found 6 were not valid

We examined 31 expenses for the employee totalling $3,440 and found that the expenses were appropriately approved and appeared valid—based on the supporting evidence. We did further work, such as confirming the nature of trips claimed with third parties, for 10 of the 31 expenses. We found the following:

Violation of the Code and the Supplement

- The employee violated the Code and the Supplement by performing fee-for-service work at a College. The employee received $600 for providing instructional services to the College and was also paid by the Department for that work day. The employee signed his annual performance contract indicating he understood the Code and the Supplement. The employee told us that he received similar payments for providing instructional services for at least three years.

Six expense claims (totalling $1,322) were either misrepresented by the employee or not confirmed by third parties

- The employee was reimbursed for mileage and meals of $40 through both the Department and the College for the trip to the College to fulfill the fee-for-service contract.
- For one expense claim that related to a training workshop (totalling $313), a third party stated that the employee was not registered in the workshop and the third party did not see him at the workshop. The third party also stated that the employee had contacted him to "vouch" for him and confirm that the employee attended the workshop as stated in the claim.

- For two expense claims (totalling $876) for trips to conduct field inspections and meetings, third parties were unable to confirm whether the meetings took place.
- Two claims where the employee claimed mileage and meals (totalling $93) for two meetings in Nisku that actually took place in Edmonton.

Other claims

For two expense claims (totalling $396), third parties verified that the meetings took place as represented by the employee. For two other expense claims (totalling $66) for out-of-town meetings, we were unable to reach the third party to verify that the meetings took place.

The Department is now reviewing our audit findings and needs to determine its next steps.

Implications and risks if recommendation not implemented

Without policies for reporting and dealing with alleged employee misconduct, Department staff may not report employee misconduct and the Department may not handle allegations consistently and thoroughly. Failure by the Department to act promptly on alleged or confirmed misconduct can affect staff's perception of acceptable behavior.

2. Department's systems for approving employee expense claims

Background

Policies exist

The Department has expense-claim policies on travel and subsistence, claiming mileage, approvals required before traveling, employee responsibilities, expenditure officer responsibilities, and hosting and working sessions.

Criteria: the standards we used for our audit

- Expense claim policies and procedures should be well-defined.
- Expense claims should be valid, supported, comply with Department policies, and approved by appropriate individuals.

Our audit findings

Policies are appropriate and complied with

Employee expense-claim policies and procedures are comprehensive and well-defined. We examined 23 expense claims for 12 department staff and found that the claims were appropriately approved, valid and supported. They also complied with Department policies.

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